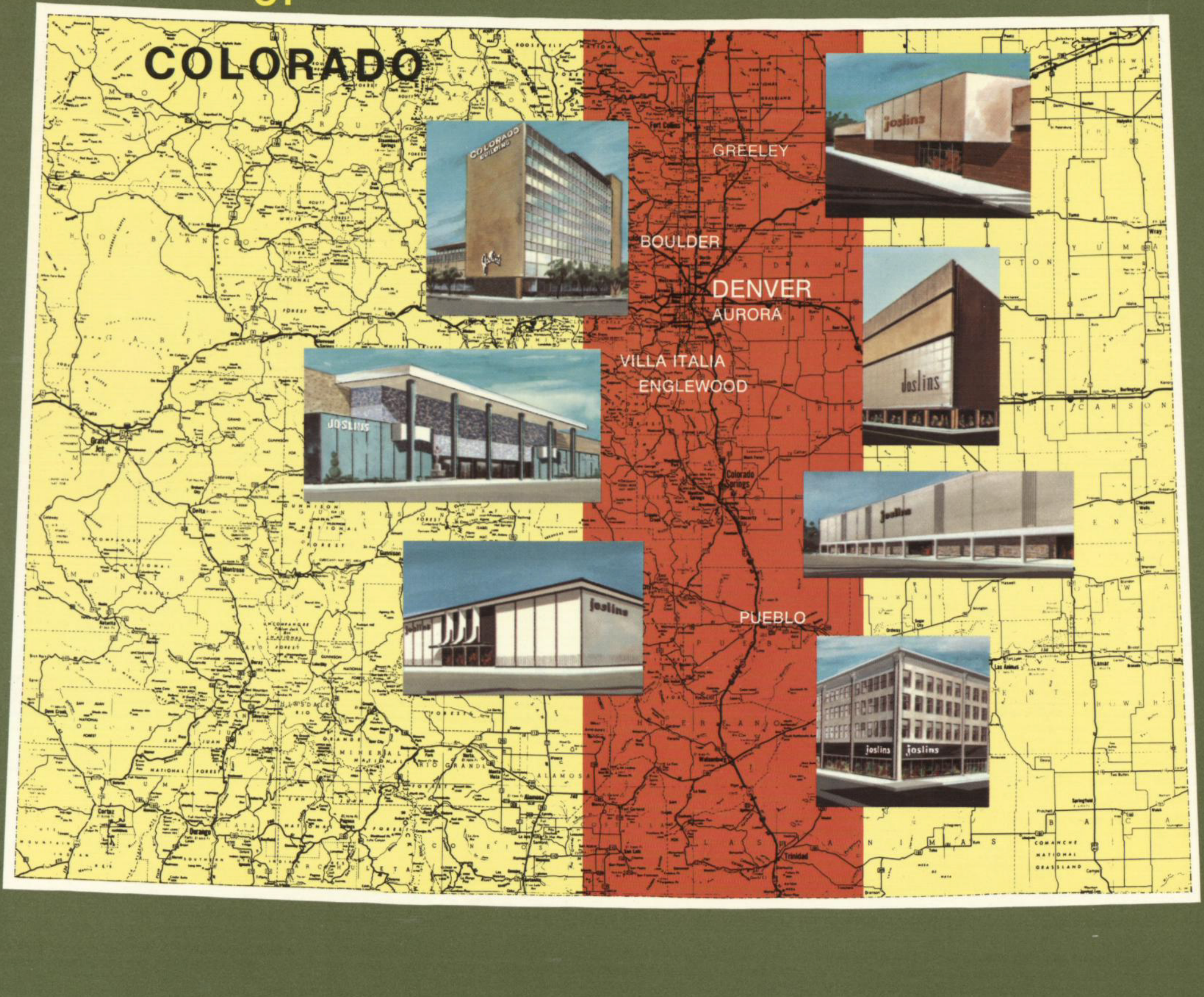
Mercantile Stores Company, Inc. Annual Report 1973

joslins
OF


COLORADO
GREELEY
BOULDER
DENVER
AURORA
VILLA ITALIA
ENGLEWOOD
PUEBLO
joslins

Contents

1 *Directors and Officers*

2 *Letter to the Stockholders*

4 *Financial Highlights in Brief*

5 *Financial and Operating Review*

15 *Financial Statements*

22 *Ten Year Review*

24 *Special Report — Joslins of Colorado*

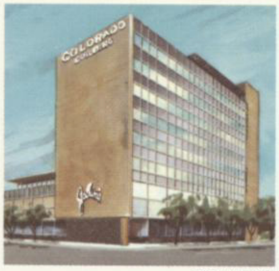
28 *List of Locations*

Annual Meeting

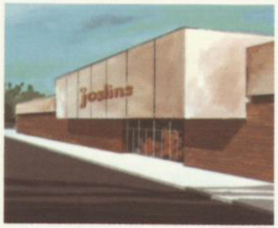
The Annual Meeting of Stockholders will be held at 11:00 a.m., on Wednesday, May 22, 1974 at 100 West 10th Street, Wilmington, Delaware. All stockholders are cordially invited to attend.

Mercantile Stores Company, Inc.

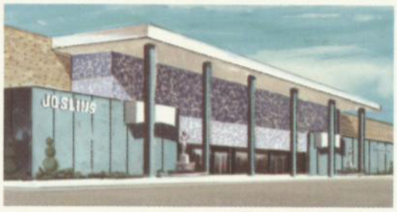
100 West 10th Street—Wilmington, Delaware



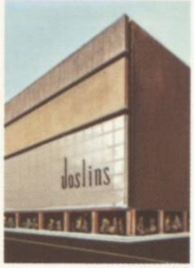
BOULDER



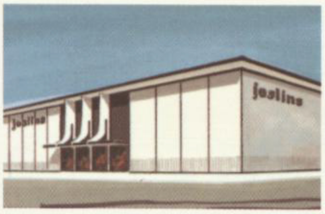
GREELEY



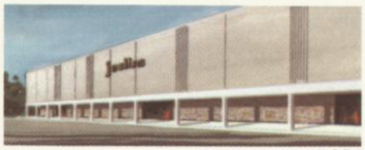
VILLA ITALIA



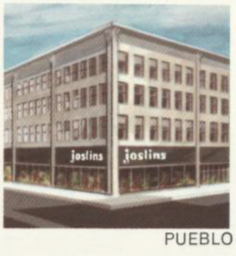
DENVER



ENGLEWOOD



AURORA



PUEBLO

joslins
OF COLORADO

Directors

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CORPORATION FILE

John E. Bierwirth
Chairman and a director of National Distillers and Chemical Corporation.

Frederick W. Bleckwenn
Vice-President
Mercantile Stores Company, Inc.

William W. Geddes
President and Chief Executive Officer and a director of Wilmington Trust Company, Wilmington, Delaware.

Harold W. Jockers
Chairman of the Executive Committee
Mercantile Stores Company, Inc.

F. G. Kingsley
Vice-President and a director of Deering Milliken, Inc.

Gerrish H. Milliken
Vice-President and a director of Deering Milliken, Inc.

Minot K. Milliken
Vice-President, Treasurer and a director of Deering Milliken, Inc.

Roger Milliken
President and a director of Deering Milliken, Inc.

George S. Moore
Director of White, Weld & Co. Incorporated and a director of White, Weld & Co. Limited.

Edward J. Sharkey
Vice-President
Mercantile Stores Company, Inc.

R. Nelson Shaw
Chairman of the Board
Mercantile Stores Company, Inc.

Charles E. Stallings
Vice-President
Mercantile Stores Company, Inc.

Leon F. Winbigler
President
Mercantile Stores Company, Inc.

Officers

R. Nelson Shaw
Chairman of the Board

Leon F. Winbigler
President

Harold W. Jockers
Chairman of the Executive Committee

F. G. Kingsley
Chairman of the Finance Committee

Frederick W. Bleckwenn
Vice-President

William A. Heineman
Vice-President and Treasurer

Edward J. Sharkey
Vice-President

Charles E. Stallings
Vice-President

Walter H. Bosch
Controller

Dennis F. Murphy
Secretary

To Our Stockholders

April 19, 1974

Sales for the year ending January 31, 1974 were up by 13%. However, the improvement in earnings in 1973 was at a lower rate than that experienced in the past several years.

Sales

$518,106,000.

Net Earnings

$21,625,000, an increase of 4.2%.

The new stores opened during 1973 affected our profits to a greater extent than stores opened in earlier years.

When one of our new stores opened last Spring, the center was incomplete and sales were disappointing for a substantial portion of the year. At the present time, the shopping center is nearly completed and we feel confident that we will see an improvement in 1974.

In another case, we became part of a major center as a defensive move to protect our dominance in the area. We realized at the time of our decision that the store would underperform at the beginning and also affect sales and profits in our downtown store, but felt it was a move that had to be undertaken.

Another reason for our modest increase was Phase IV regulations which hampered our overall profit margins. Lower mark-ups in certain categories could not be used to offset those categories with higher margins which had to be reduced by year-end to comply with the regulations. This, in our opinion, needlessly reduced our profit margins.

The Financial and Operating Review which follows this letter details our operations during the year.

Merchandising Policy

In everything we do, our first concern is how best we can satisfy our customers and attract others. We offer price ranges appealing to the greatest number, stressing quality merchandise at reasonable prices. Value is the key word, not price.

Emphasis is placed on the importance of balanced stocks in size and color. Nothing aggravates a customer more than to be unable to purchase her size or color in a particular item.

We believe in presenting the newest and most interesting fashions that anyone might expect to find in his or her favorite department store. Famous names throughout the store make a good store more attractive and exciting. We have a wide variety of national brands in all departments. Over the past several years, we have broadened our emphasis on national brands and styling and will continue to do so because we believe that the consumer is becoming more and more discriminating.

Of equal importance to us is the wide assortment of our *own* private brands of quality merchandise at very competitive prices. Over the years our customers have come to recognize their outstanding value. In men's and boy's wear, our name is Royal Knight; in women's wear Merville; in girl's and infant's Royal Deb and Royal Heir; and in home furnishings First Lady.

Service to Our Customers

We do not pay lip service to the axiom that "the customer is always right."

Shopping in our stores should always be pleasant and our sales staff is trained to make this a reality. We strive to do everything which will allow our sales people and department managers to spend as much time on the selling floor as possible in order to service our customers.

Customers find that our policy in regard to returns and exchanges is extremely liberal. Any sales person can handle the transaction, including issuing a credit refund or cash disbursement on the selling floor. It is no more difficult to make a return than to make a purchase.

Our Personnel

Our greatest asset is our loyal and hard working staff, many of them with a lifetime of service to the Company.

We believe that this dedication is to a large measure a result of our long established policy of promotion from within. At all levels, we have our share of capable associates who have started as trainees. We rarely go outside the Company to fill a position of responsibility.

Directors and Officers

No two finer examples of dedication to the Company can be found than in Mr. F. Kenneth Bradley and Mr. Morgan A. Casey who resigned as Directors in February, 1974.

Mr. Bradley started with the Company in 1935, becoming a Vice President and Director in 1947, President in 1960 and Vice Chairman in 1964.

Mr. Casey commenced his employment in 1936, was appointed Treasurer in 1941, a Director in 1951 and Vice President in 1956.

These two gentlemen formed part of a uniquely blended management team that evolved the principles that enabled the Company to weather the economic storms of the thirties and are responsible for the growth that has ensued since then.

We deeply regret to record the death of Mr. Abbott D. Churbuck in March, 1974.

Mr. Churbuck joined the Company in 1935, becoming Vice President in 1941 and a Director in 1951, retiring in 1965 after 30 years of unstinting devotion to the Company's affairs. His contribution to the Company during those difficult years is immeasurable. But Mr. Churbuck will be remembered best for his gentle manner, even in times of stress, and his quick laughter, sometimes at himself. We shall miss him.

In December, 1973, Mr. Leon F. Winbigler was appointed President and a Director of the Company.

Mr. Winbigler, 48 years of age, has been with the Company for 25 years. He managed the Root Dry Goods Company in Terre Haute, Indiana in 1953 and 1954, the MacDougall and Southwick Division in Seattle, Washington from 1954 to 1962, and the Lion Dry Goods Company in Toledo, Ohio from 1962 until his appointment as President of the Company.

At the April 4, 1974 meeting of the Board of Directors Mr. Frederick W. Bleckwenn and Mr. Edward J. Sharkey were appointed Directors.

Mr. Bleckwenn, 58, is a Vice President of the Company mainly responsible for the Credit and Data Processing operations while Mr. Sharkey, 48, as Vice President directs the Real Estate and Store Planning division.

Mr. Dennis F. Murphy, 37, who is responsible for the Tax and Insurance programs of the Company, was elected Secretary in February, 1974.

Joslins of Colorado

Joslins is featured in our special report this year. Under the able and innovative leadership of Mr. Donald Chabot, great things have been happening.

Recent Trend

Sales for February increased by 10.4%. March was up by 13.6% for a year-to-date increase of 12.4%.

Respectfully submitted,

R. Nelson Shaw

R. Nelson Shaw, *Chairman of the Board*

L. F. Winbigler

Leon F. Winbigler, *President*

By Order of the Board of Directors

Financial Highlights in Brief

	1973 *(Year Ended Jan. 31, 1974)*	1972 *(Year Ended Jan. 31, 1973)*
Operating Results:		
Net sales	**$518,106,000**	$458,328,000
Sales increase percentage	**13.0%**	16.5%
Income before Federal income taxes	**40,695,000**	39,156,000**
Percent to sales	**7.9%**	8.5%
Net income	**21,625,000**	20,756,000**
Percent to sales	**4.2%**	4.5%
Per Common Share:*		
Net income	**$3.67**	$3.52**
Dividends	**.77½**	.70
Financial Position:		
Working capital	**$ 95,248,000**	$ 88,127,000
Ratio of current assets to current liabilities	**2.47**	2.73
Receivables — net	**13,960,000**	18,225,000
Due from Mersco Finance Corporation	**47,257,000**	28,493,000
Inventories	**87,139,000**	79,975,000
Property and equipment — net	**93,907,000**	87,368,000
Total assets	**260,529,000**	229,813,000
Long-term debt	**32,799,000**	34,243,000
Stockholders' equity	**156,703,000**	139,647,000
Per common share*	**26.58**	23.69
Ratio of net income to invested capital	**14.6%**	15.8%
Stores at end of year	**72**	71
Total square feet	**7,372,000**	6,863,000

*1972 per share figures adjusted to reflect 2 for 1 split in 1973.

**Included in the net income for 1972 is a gain on sale of land of $414,000 equal to $.07 per share.

Financial and Operating Review

Sales

Sales for the year ended January 31, 1974 totaled $518,106,000, an increase of 13% over the previous year's $458,328,000. This was the 18th consecutive year in which sales showed an increase over the preceding year and the first year in which sales exceeded the half billion dollar mark.

The Company, directly or through wholly owned subsidiaries, operates 67 department stores in the downtown and suburban areas of cities in 18 states of the United States and 5 stores in the Province of Ontario, Canada. All stores operate under locally prominent trade names and stress a wide selection of goods and a high degree of service. A listing of our stores begins on page 28 of this report.

Sales in stores opened prior to February 1, 1972 with no appreciable change in square footage during the last 2 years (which we refer to as comparable stores) had an increase of 6%.

Net Sales (thousands)

Quarter	1973	1972	Percent Increase
1st	$102,645	$ 87,378	17.5
2nd	116,280	100,030	16.2
3rd	123,858	112,418	10.2
4th	175,323	158,502	10.6
	$518,106	$458,328	13.0

Sales outside of the Company's central downtown area stores accounted for 80% of the total net sales.

A relatively small proportion of the Company's business is conducted through departments leased to others. During the year ended January 31, 1974, these sales were $11,621,000 which represented 2% of total net sales.

Earnings

Net income from all operations amounted to $21,625,000, an increase of 4.2% over the record earnings of $20,756,000 for the prior year (which included a non-recurring gain of $414,000 largely from the sale of land no longer useful in the business).

Per share earnings were $3.67. Last year the Company earned $3.52 which included 7¢ for the non-recurring gain mentioned above. All share and per-share amounts in this Annual Report have been adjusted for the 2 for 1 stock split approved on May 23, 1973.

Income before Federal income taxes increased to $40,695,000, representing 7.9% of sales compared to $39,156,000, or 8.5% of sales, in 1972.

Net Income (thousands)

	1973		1972	
Quarter	Amount	Per Share	Amount	Per Share
1st	$ 3,183	$ .54	$ 2,757	$ .47
2nd	2,986	.51	2,731	.46
3rd	4,510	.76	4,673	.79
4th	10,946	1.86	10,595	1.80
	$21,625	$3.67	$20,756	$3.52

The investment tax credit this year was $785,000, or 13¢ per share, an increase of $116,500 over last year's $668,500 or 11½¢ per share.

Next year we expect a substantial drop in the investment tax credit because of the slower expansion pace.

Fourth Quarter Results (thousands)

	Three Months Ended January 31, 1974	Three Months Ended January 31, 1973
Net sales	$175,323	$158,502
Income before Federal income taxes	$ 19,826	$ 19,145*
Federal income taxes	8,880	8,550
Net income	$ 10,946	$ 10,595*
Net income per share	$ 1.86	$ 1.80*

* Includes a gain on sale of land of $414,000, or 7¢ per share.

A substantial portion of the investment tax credit is reflected in the fourth quarter, resulting in a lower effective tax rate for that quarter as compared to the effective tax rate for the year.

Dividends

The Company has only one class of stock—common. At the Annual Meeting held on May 23, 1973, the stockholders approved a split of the stock on the basis of two shares for one. As a result, there are now 5,901,996 shares issued, of which 5,895,636 shares are outstanding and 6,360 are held in treasury. There are approximately 5,300 stockholders.

The Company made the following dividend payments during the year.

March 15, 1973	$.17½
June 15, 1973	.20
September 15, 1973	.20
December 15, 1973	.20
	$.77½

Dividends totaled $4,569,000, representing 21% of net income.

Cash, Compensating Balances and Debt

The Company maintains important banking relationships with a number of banks throughout the country, principally with the First National City Bank of New York.

The Company must rely on short term borrowings during most of the year until such time as cash is generated during the Christmas season.

The Company relies primarily upon the sale of its customer receivables to provide short term funds. It accomplishes this financing by selling its receivables, without recourse, to its wholly owned subsidiary, Mersco Finance Corporation, which withholds, as a reserve, an amount equal to 10% of the receivables so acquired.

Mersco Finance Corporation has a credit agreement with First National City Bank under which it can borrow up to a total of $12,000,000 from time to time up to and including January 31, 1975. Any amount outstanding at that date is to be paid in sixteen substantially equal quarterly installments commencing April 30, 1976.

In addition, Mersco Finance Corporation has an open line of credit with First National City Bank under which it can borrow up to a total of $30,000,000. These borrowings are evidenced by unsecured notes, payable on demand.

At January 31, 1974, all borrowings under these arrangements had been repaid. During the fiscal year, the maximum borrowings outstanding at any month end amounted to $31,000,000. Average monthly borrowings totaled $20,958,000 with an average interest rate (based on the prime rate of the bank) of 7.9%. A commitment fee of $5,000, based on ½ of 1% per annum on the average daily unused portion of the commitment, was charged under the $12,000,000 credit agreement.

The Company also has an open line of credit with First National City Bank under which it can borrow up to a total of $25,000,000 at the prime rate of interest. During the current fiscal year, the Company did not find it necessary to avail itself of this line of credit.

The Company has an informal understanding with First National City Bank that it will maintain average collected balances in its accounts with the bank of 10% of the total available borrowings ($67,000,000). An additional 10% will be maintained for any sums borrowed in excess of $33,500,000. The average collected balances exceeded the average book balances during the year by approximately $3,000,000 due to the excess of unpresented checks over uncollected deposits. Accordingly, an average of approximately $3,700,000 of cash included in the Company's books was maintained in support of this arrangement. The lines of credit, but not the credit agreement, may be withdrawn at any time at the option of the bank.

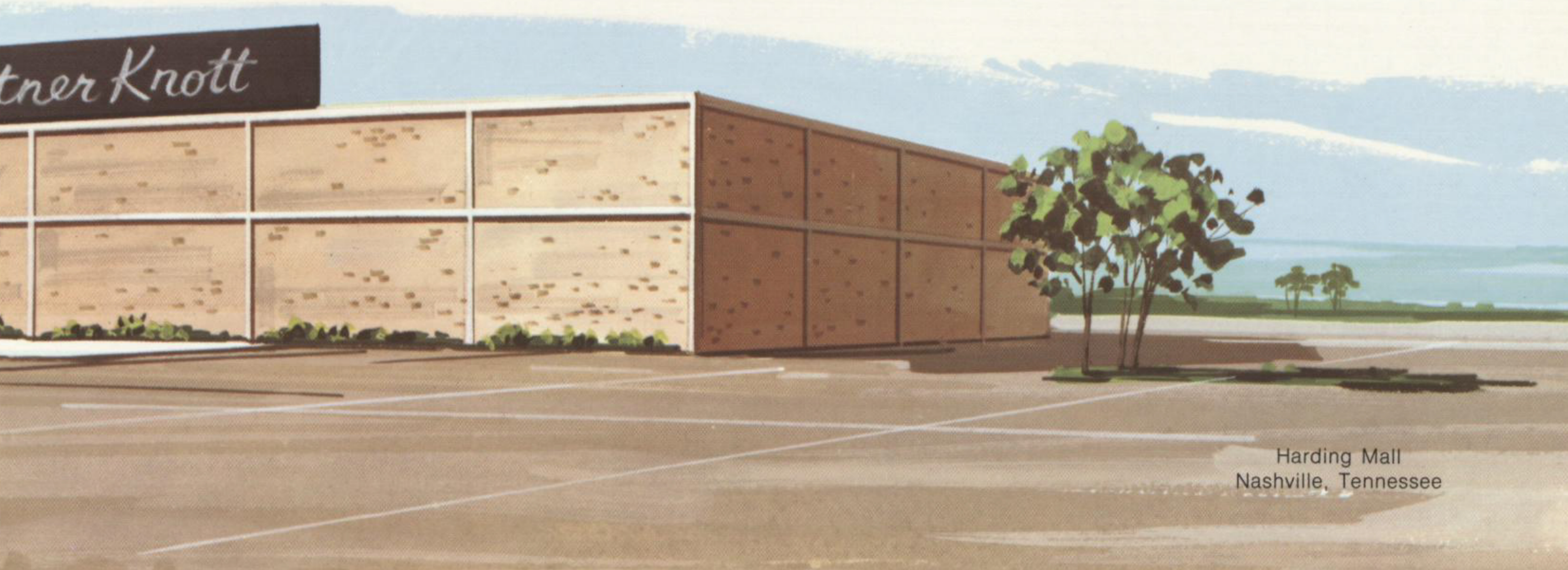
While the balances are maintained in accordance with the above described arrangement, it is meaningful to mention that the bank balances also compensate the bank for the services rendered to the Company throughout the year.

From time to time, because of existing relationships, other banks offer lines of credit which are accepted by the Company without any intention at that time to use such lines.

No long-term debt was incurred by the Company and its consolidated subsidiaries in 1973.

Debt outstanding was as follows:

	January 31, 1974	January 31, 1973
8.70% Sinking Fund Debentures due 1995	$25,000,000	$25,000,000
5⅛% Notes due 1978—$333,000 due annually, $338,000 due December 1, 1977, with $2,500,000 due December 1, 1978	3,837,000	4,170,000
4% to 6⅛% Mortgage Notes—Generally payable quarterly over the life of the mortgage	5,406,000	6,502,000
	$34,243,000	$35,672,000
Less—due within one year	1,444,000	1,429,000
	$32,799,000	$34,243,000



Harding Mall
Nashville, Tennessee

Maturities on long-term debt for the next 5 years are as follows:

Year Ending	Amount
January 31, 1975	$1,444,000
January 31, 1976	1,383,000
January 31, 1977	2,469,000*
January 31, 1978	2,159,000*
January 31, 1979	4,116,000*

* Includes annual sinking fund payment of $1,250,000 commencing December 1, 1976.

In the year under review, interest costs increased by $639,000 due mainly to the higher short term interest rates which prevailed during most of the year. Interest expense was nevertheless helped by the use of the deferred income taxes on installment sales which the Company availed itself of for the first time in its handling of receivables on its income tax returns.

Substantially all of the income before income taxes of Mersco Finance Corporation is used to reduce interest expense of the Company and is so reflected on the Company's statements of consolidated income.

Expansion

During the year, the Company opened the following stores:

Location	Sq. Ft.	Opening Date
Clearwater, Florida	142,500	April 5, 1973
Duluth, Minnesota	146,000	July 26, 1973
Greeley, Colorado	93,250	June 30, 1973
Auburn, Alabama	93,250	August 1, 1973

The smaller units at Greeley, Colorado and Opelika, Alabama with a combined area of 53,250 sq. ft. were closed prior to the opening of the larger units in Greeley and Auburn.

The Company also closed a small store (35,700 sq. ft.) in Independence, Missouri at the end of December, 1973.

Two stores were expanded. An additional 50,000 sq. ft. was added to the Harding Mall store in Nashville, Tennessee and 55,500 sq. ft. to the National Hills store in Augusta, Georgia.

In addition to the above, the Company opened a small specialty store with about 17,000 sq. ft. in the Crown Center in Kansas City, Missouri on September 24, 1973. There are no present plans to do anything similar elsewhere.

In 1974, the Company will pursue a very modest expansion program, enlarging two stores; one in Edgewater, Mississippi and the other in Tuscaloosa, Alabama. In both cases, 80,000 sq. ft. will be added, to

double them in size. The Company would have preferred one or two new store openings in 1974 but a delay in closing certain real estate transactions precluded any new stores for next year.

Plans are going forward for the opening of four stores in 1975; two with 90,000 sq. ft. each, one with 100,000 sq. ft. and the other with 140,000 sq. ft. A similar pattern is planned for 1976.

Pre-opening expenses (including interest and real estate taxes during construction) are expensed as they are paid prior to opening and, insofar as practicable, those not paid are accrued and charged against the operation in the month in which the store opens.

On January 31, 1973, the Company reported 6,863,400 sq. ft. of gross space, exclusive of segregated warehouse facilities. Four new stores and the specialty store added 492,000 sq. ft. and the expanded stores 105,500 sq. ft., for a total of 597,500 sq. ft. The three small units closed had a combined footage of 88,950. The net addition of 508,550 sq. ft. brought the total at year end to 7,371,950 sq. ft.

Property and Equipment

The Company expended $16,072,000 for plant and equipment during the year which was $3,694,000 less than that spent in the prior year.

Planned capital expenditures for the new year have been budgeted at $15,000,000 in view of the slower pace of expansion for 1974.

Changes in Property and Equipment (thousands)

	1973	1972
Balance—Beginning of Year	$87,368	$76,538
Additions at Cost	16,072	19,766
Depreciation	(9,533)	(7,557)
Dispositions	—	(1,379)
Net Increase for Year	6,539	10,830
Balance—End of Year	$93,907	$87,368

Depreciation for the year amounted to $9,533,000 on a straight-line basis, an increase of $1,976,000 over that provided in 1972.

Maintenance and repairs totaled $1,879,000, all of which was expensed.

Leases and Commitments

The Company had 120 leases in effect at January 31, 1974, most of which will expire during the next twenty years. In the normal course of business, it is expected that many of them will be renewed or replaced by leases on other properties.

The Company has classified its lease commitments as either "financing" leases or "operating" leases. In general, a financing lease is defined as a lease which during the noncancelable lease period, either (1) covers

Tuscaloosa, Alabama

75% or more of the economic life of the property or (2) has terms which assure the lessor full recovery of the fair market value of the property plus a reasonable return.

Rent expense on leases, primarily real estate, was as follows (in thousands):

	1973		
	Financing Leases	**Operating Leases**	**Total**
Minimum Rentals	$4,062	$1,427	$5,489
Contingent	1,030	145	1,175
Total Rent Expense	$5,092	$1,572	$6,664

	1972		
	Financing Leases	**Operating Leases**	**Total**
Minimum Rentals	$3,120	$1,466	$4,586
Contingent	974	183	1,157
Total Rent Expense	$4,094	$1,649	$5,743

Contingent rentals are based on percentages of sales.

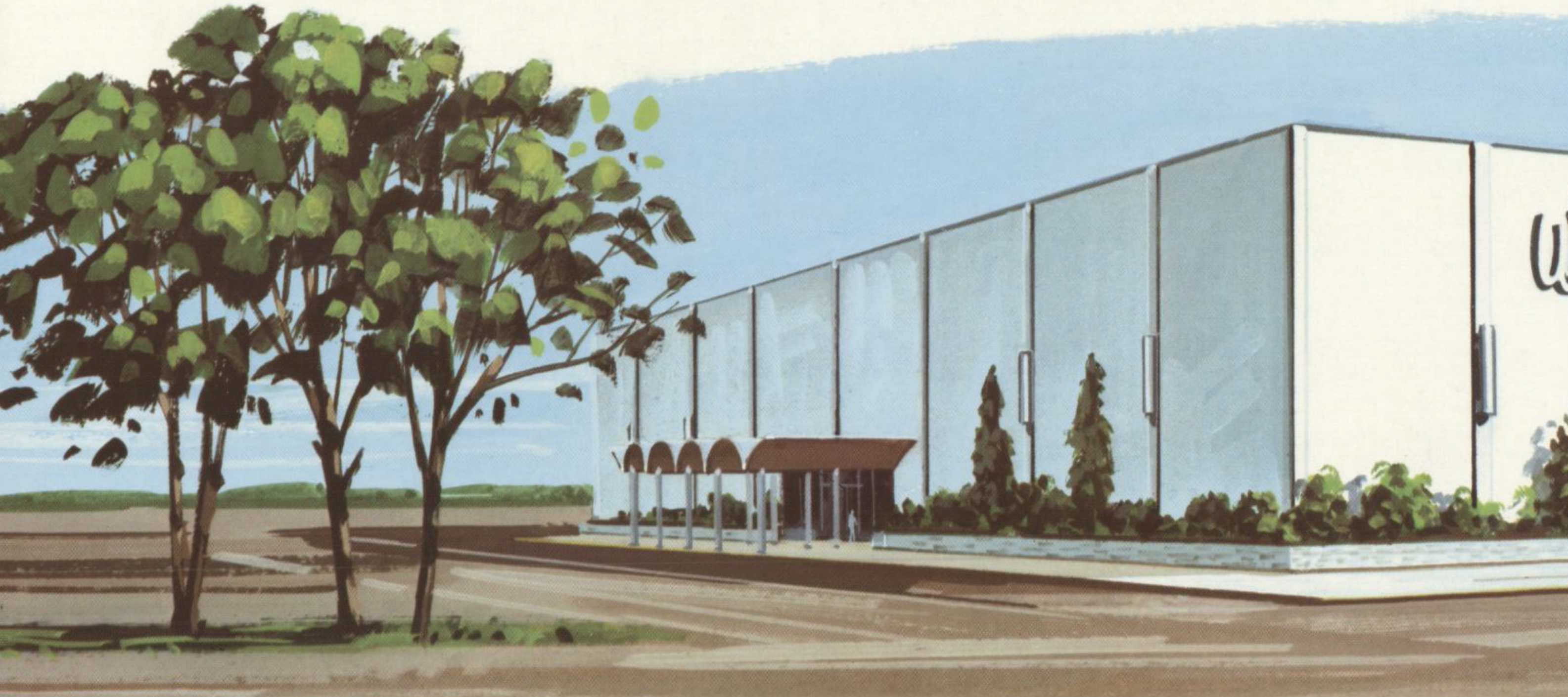
The future minimum annual lease commitments on noncancelable leases in effect at January 31, 1974, (in thousands), were as follows:

Fiscal years Ending Jan. 31st	**Financing Leases**	**Operating Leases**	**Total**
1975	$ 4,745	$1,217	$ 5,962
1976	4,723	1,088	5,811
1977	4,723	941	5,664
1978	4,723	857	5,580
1979	4,696	673	5,369
1980-84	23,324	2,193	25,517
1985-89	20,968	401	21,369
1990-94	15,775	95	15,870
After 1994	13,833	790	14,623
	$97,510	$8,255	$105,765

Many of the leases require additional payments for real estate taxes and insurance in addition to the contingent rentals.

The present values of the aggregate minimum lease commitments relating to the financing leases and the interest rates used in the computations were as follows:

Ranges Of Interest Rates Used In The Present Value Computation	**Weighted Average Interest Rate Year Ending January 31,**		**Present Value Of Rentals At January 31, (thousands)**	
	1974	**1973**	**1974**	**1973**
4.50-9.88%	6.81%	6.06%	$42,091	$36,048



If the financing leases were capitalized, with the lease rights amortized on a straight-line basis and interest expense accrued on the outstanding lease liability, net income for the years ended January 31, 1974 and January 31, 1973 would not have been materially affected.

Book and Tax Income

The Statements of Consolidated Income for the years ended January 31, 1974 and January 31, 1973 reflect Federal income taxes of $19,070,000 and $18,400,000, respectively. This includes amounts currently payable and amounts deferred as follows:

(thousands)	1973	1972
Currently Payable	$16,854	$10,788
Deferred	2,216	7,612
	$19,070	$18,400

Deferred tax expense results from timing differences in the recognition of revenue and expense for tax and financial statement purposes. The sources of these differences and the tax effect of each were as follows:

(thousands)	1973	1972
Excess of tax over book depreciation	$1,077	$1,012
Income deferred for tax purposes on installment sales to customers but recognized as income on the books	1,139	6,600
	$2,216	$7,612

In both years total tax expense was slightly less than the amount computed by applying the U. S. Federal income tax rate of 48% to income before tax. The only significant reason for these differences was the investment tax credits of $785,000 in 1973 and $668,500 in 1972, which are treated as a current reduction of Federal income taxes.

Pension and Profit Sharing Plans

The Company established its Pension Plan on February 1, 1945 and from its inception has paid all the costs associated with it.

The Savings and Profit Sharing Plan was instituted on February 1, 1954, and during its 20 years of operation the Company turned over to the Trustee $13,734,000 from its profits for the benefit of the participants.

National Hills
Augusta, Georgia

The expenses of the Company for the latest two years were as follows:

(thousands)	1973	1972
Pension	$1,832	$1,507
Savings and Profit Sharing	1,921	1,840
	$3,753	$3,347

The latest report of the actuary, as of January 31, 1973, stated that employees' vested benefits were fully funded and that unfunded prior service costs, which are being amortized over 10 years, amounted to $3,250,000. Accrued pension costs are funded currently.

Employees with 2 years of service who have reached their 25th birthday are eligible for both plans. Induction into the Pension Plan, being non-contributory, is automatic but the employee must indicate his desire to join the Savings and Profit Sharing Plan by agreeing to contribute 2, 4, 6, 8 or 10% of his annual earnings through payroll deductions.

At year-end, there were 5,018 participants in the Pension Plan. The plan, managed by First National City Bank as Trustee, had a market value of $13,775,000.

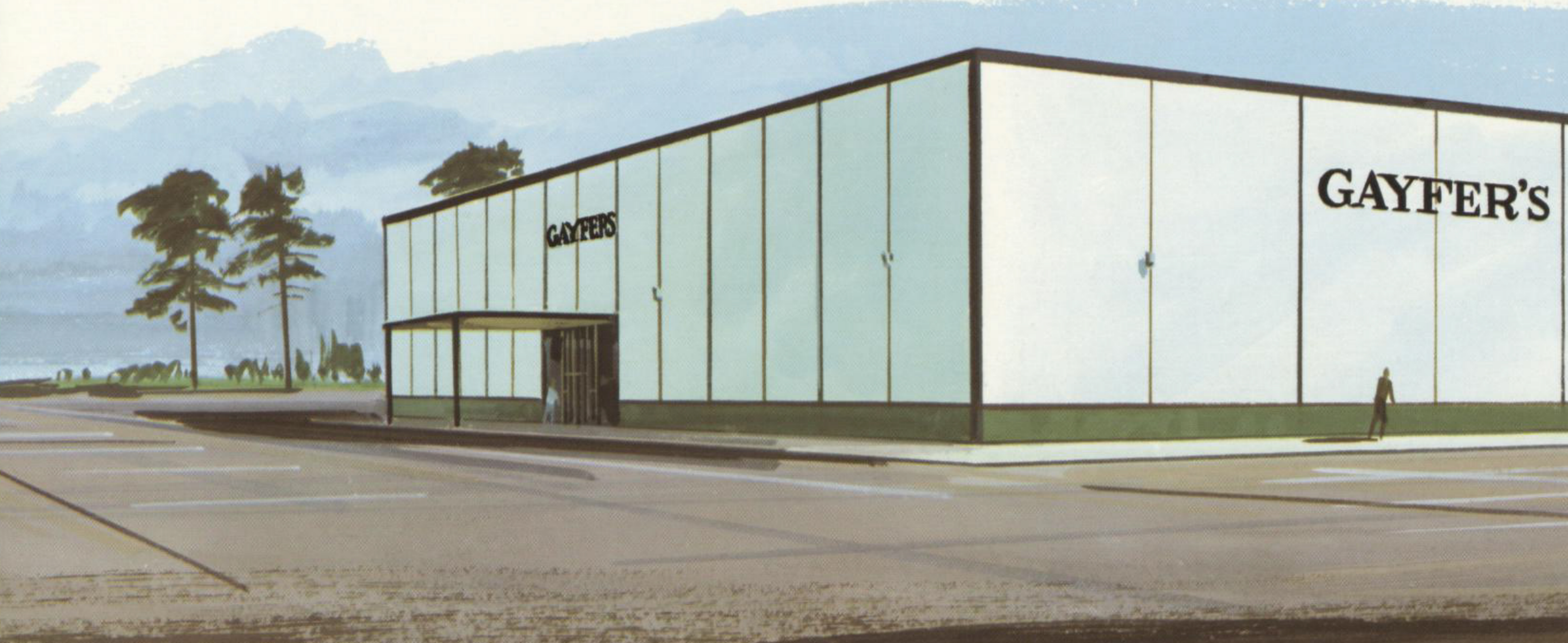
The Savings and Profit Sharing Plan is comprised of two funds: one representing contributions by the employees invested in equity and fixed income securities which had a market value of $18,750,000, and the other representing contributions by the Company invested in Mercantile Stores common stock with a market value of $15,882,000 at year-end.

The fund holding the Company's contributions owned 393,600 shares of Mercantile common stock which represented 6.7% of its outstanding shares.

The contribution by the Company this year meant that each participant received 76¢ for each $1.00 contributed up to 6% of his earnings (any contribution in excess of 6% is not considered in apportioning the Company's contribution).

Receivables and Credit

Credit sales increased by almost $23,000,000 and represented 43.4% of total sales, down from 44.0% last year. Early in the year, we anticipated changes in economic conditions by raising our standards for granting credit. In addition, we started a program of automating credit authorization to control account balances. A third program, started in the fall, was a change in payment terms requiring larger monthly payments on



the larger balance Revolving Charge Accounts.

The combination of these three programs resulted in a smaller growth in receivables than occurred last year. Receivables (in thousands) were as follows:

	January 31, 1974	January 31, 1973
Customer Accounts		
Regular Retail	$10,426	$ 9,087
Revolving Charge	47,189	45,525
Installment	9,130	7,941
	$66,745	$62,553
Less: Reserve for Doubtful Accounts	(3,671)	(3,449)
Accounts Sold to Mersco Finance Corporation, Net of Retained Equity of $5,775,000 and $5,250,000, respectively	(51,975)	(47,248)
Customer—Net	$11,099	$11,856
Other	2,861	6,369
Receivables—Net	$13,960	$18,225

With the change in payment terms and an aggressive collection follow-up monthly, collections in general were better than last year. Bad debt losses remained at the same percent to credit sales level as in recent years. Delinquency, at a low percent to outstanding receivables, is comparable with last year.

We intend to continue the program of automating credit authorization procedures in the Company.

Our reserve for doubtful accounts continues at 5½% of our outstanding customer receivables.

Inventory

Inventories at year-end totaled $87,139,000, an increase of 9% over last year's closing inventory.

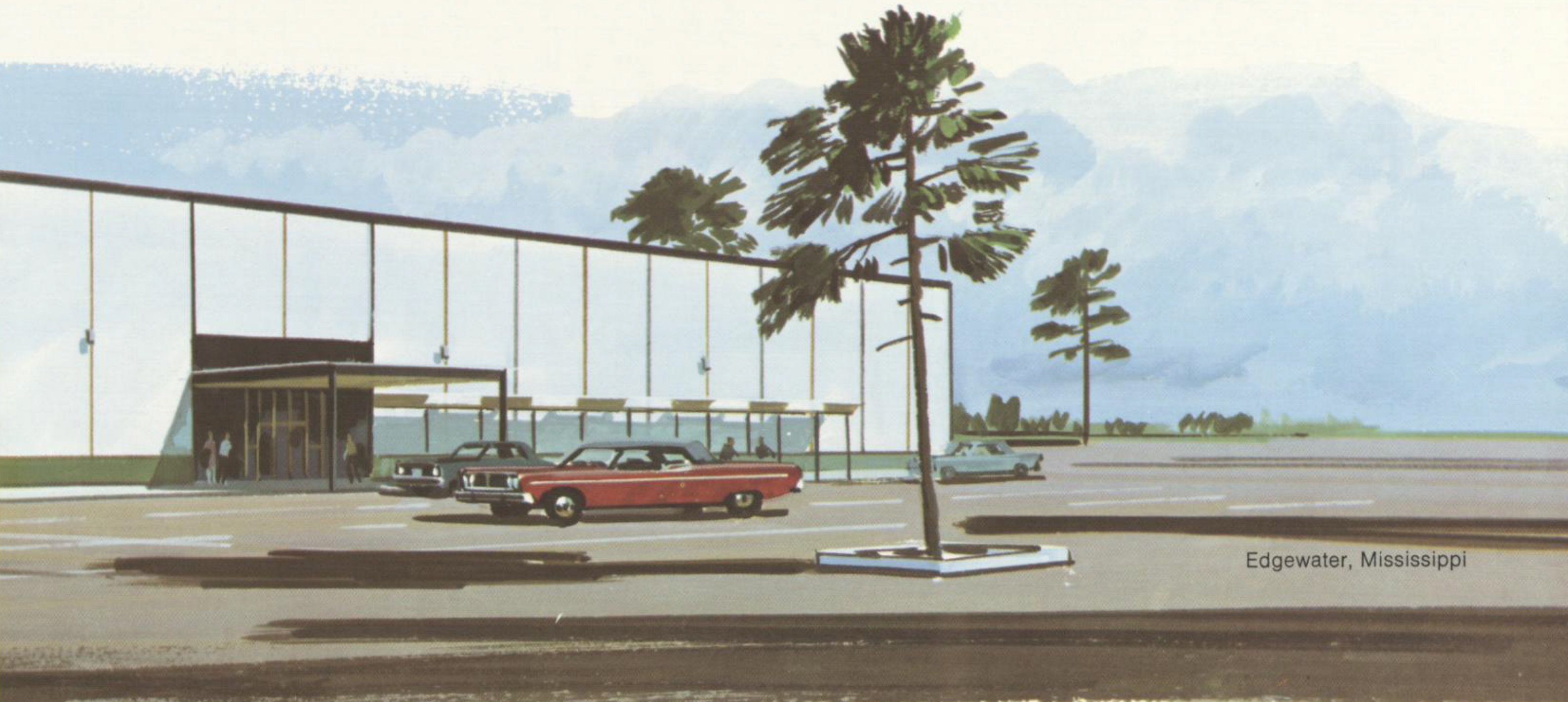
Inventories are valued at cost or market, whichever is lower, as determined by the retail inventory method. A complete physical inventory is taken at year-end. A semi-annual inventory is required of those stores whose preceding year-end inventory reflects shrinkage considered higher than normal. In addition, certain departments are inventoried at various times during the year.

Shrinkage (unaccounted losses between the physical and book inventories) remained at a very satisfactory level.

Stockholders' Equity

Equity capital increased to $156,703,000 at fiscal year end.

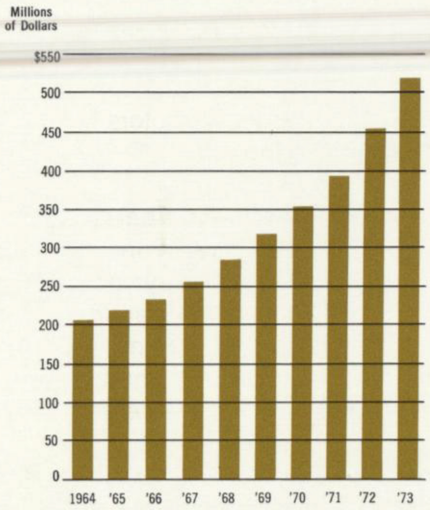
The book value per share of the Company's stock was $26.58 compared with $23.69 at the close of 1972.



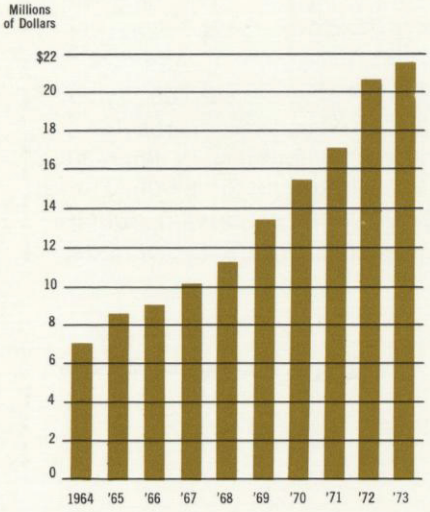
Edgewater, Mississippi

A Decade of Growth

NET SALES

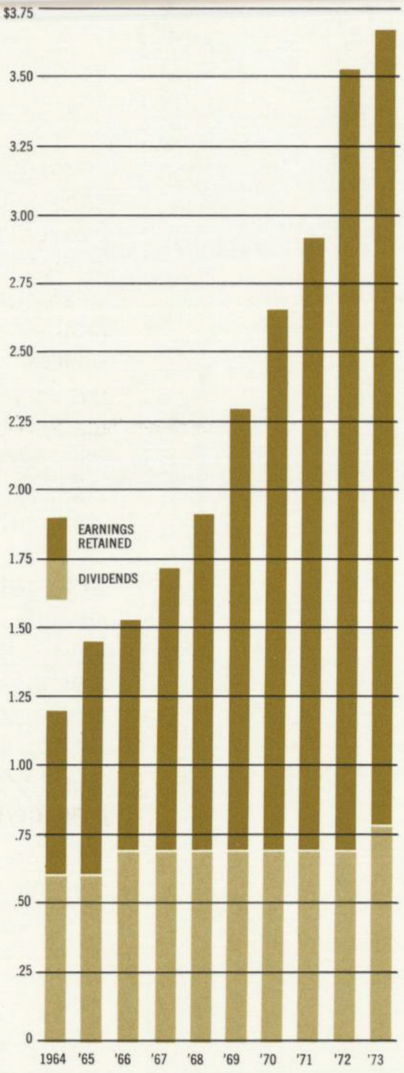


NET EARNINGS*



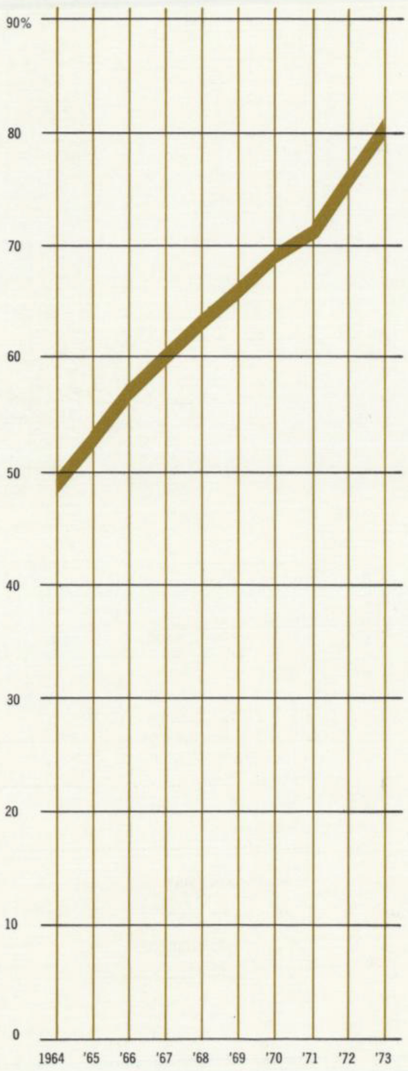
*NOT INCLUDING EXTRAORDINARY ITEMS.

EARNINGS*, DIVIDENDS AND RETAINED EARNINGS* PER SHARE OF STOCK



*NOT INCLUDING EXTRAORDINARY ITEMS.

SUBURBAN STORE SALES % OF TOTAL SALES



Financial Statements

Auditors' Report

To the Stockholders and Board of Directors of
Mercantile Stores Company, Inc.:

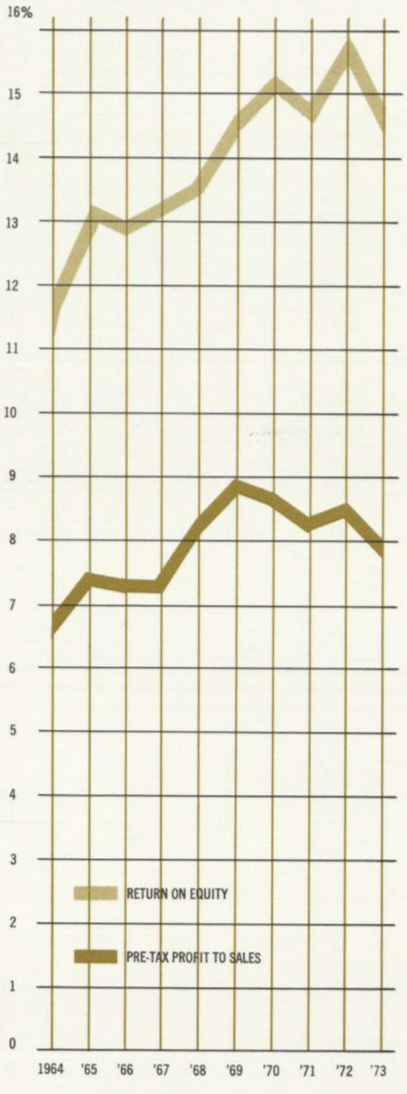
We have examined the consolidated balance sheets of Mercantile Stores Company, Inc. (a Delaware corporation) and subsidiary companies as of January 31, 1974 and 1973, and the related statements of consolidated income and retained earnings and changes in financial position for the years then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, the consolidated financial statements referred to above present fairly the financial position of Mercantile Stores Company, Inc. and subsidiary companies as of January 31, 1974 and 1973, and the results of their operations and the changes in financial position for the years then ended, in conformity with generally accepted accounting principles consistently applied during the periods.

Arthur Andersen & Co.

New York, N. Y.,
April 4, 1974.

PERCENTAGE OF PRE-TAX PROFIT
TO SALES AND RETURN ON EQUITY*



*BASED ON AVERAGE INVESTMENT

Statements of Consolidated Income and Retained Earnings

	For the years ended January 31,	
	1974	1973
Net Sales	**$518,106,000**	$458,328,000
Costs and Expenses:		
Cost of goods sold (including occupancy expenses)	**357,203,000**	314,682,000
Selling, general and administrative expenses	**115,442,000**	100,363,000
Interest expense	**4,766,000**	4,127,000
	477,411,000	419,172,000
Income Before Federal Income Taxes	**40,695,000**	39,156,000
Federal Income Taxes—see page 11:		
Currently payable	**16,854,000**	10,788,000
Deferred	**2,216,000**	7,612,000
	19,070,000	18,400,000
Net Income	**$ 21,625,000**	$ 20,756,000
Retained Earnings at beginning of year	**128,098,000**	111,469,000
	$149,723,000	$132,225,000
Cash Dividends declared and paid $.77½ and $.70 per share, respectively	**4,569,000**	4,127,000
Retained Earnings at end of year	**$145,154,000**	$128,098,000
Net Income per common share (after giving effect to 2 for 1 split)	**$3.67**	$3.52

See Notes to Consolidated Financial Statements on pages 20 and 21.

Statements of Consolidated Changes in Financial Position

	For the years ended January 31,	
	1974	1973
Sources of Working Capital:		
Net income	**$ 21,625,000**	$20,756,000
Depreciation	**9,533,000**	7,557,000
Increase in deferred income taxes	**1,146,000**	1,092,000
Funds provided from operations	**32,304,000**	29,405,000
Net proceeds from sale of land	**—**	1,379,000
Total	**32,304,000**	30,784,000
Dispositions of Working Capital:		
Dividends paid	**4,569,000**	4,127,000
Additions to property and equipment	**16,072,000**	19,766,000
Reduction in long-term debt	**1,444,000**	1,576,000
Increase in other investments	**131,000**	400,000
Increase in equity in and advance to Mersco Finance Corporation	**2,967,000**	941,000
Total	**25,183,000**	26,810,000
Increase in Working Capital	**$ 7,121,000**	$ 3,974,000
Changes in Working Capital:		
Current assets		
Cash	**($ 422,000)**	($ 4,772,000)
Receivables	**(4,265,000)**	8,352,000
Due from Mersco Finance Corporation	**18,764,000**	(2,448,000)
Inventories	**7,164,000**	14,553,000
Prepayments and other	**(162,000)**	72,000
Total	**21,079,000**	15,757,000
Current liabilities		
Accounts payable	**4,034,000**	5,292,000
Accrued liabilities	**3,391,000**	1,269,000
Federal income taxes	**5,514,000**	(1,843,000)
Deferred income taxes on installment sales	**1,004,000**	7,079,000
Debt due within one year	**15,000**	(14,000)
Total	**13,958,000**	11,783,000
Increase in Working Capital	**$ 7,121,000**	$ 3,974,000

See Notes to Consolidated Financial Statements on pages 20 and 21.

Consolidated Balance Sheets

	January 31,	
ASSETS		
Current Assets:	**1974**	1973
Cash, including certificates of deposit	**$ 9,775,000**	$ 10,197,000
Receivables — see page 12	**13,960,000**	18,225,000
Due from Mersco Finance Corporation	**47,257,000**	28,493,000
Inventories — at lower of cost or market (retail method)	**87,139,000**	79,975,000
Prepayments and other	**2,117,000**	2,279,000
Total Current Assets	**160,248,000**	139,169,000
Other Investments	**2,234,000**	2,103,000
Equity in and Advance to Mersco Finance Corporation—Note 3	**4,140,000**	1,173,000
Property and Equipment, at cost:		
Land	**8,278,000**	7,840,000
Buildings and improvements	**78,944,000**	73,683,000
Fixtures	**56,788,000**	49,297,000
	144,010,000	130,820,000
Less accumulated depreciation	**50,103,000**	43,452,000
Property and Equipment — Net	**93,907,000**	87,368,000
Total	**$260,529,000**	$229,813,000

See Notes to Consolidated Financial Statements on pages 20 and 21.

LIABILITIES AND STOCKHOLDERS' EQUITY

	January 31,	
	1974	1973
Current Liabilities:		
Accounts payable	**$ 33,221,000**	$ 29,187,000
Accrued liabilities	**15,732,000**	12,341,000
Federal income taxes	**6,520,000**	1,006,000
Deferred income taxes on installment sales	**8,083,000**	7,079,000
Debt due within one year	**1,444,000**	1,429,000
Total Current Liabilities	**65,000,000**	51,042,000
Long-Term Debt — see page 7	**32,799,000**	34,243,000
Deferred Income Taxes applicable to depreciation	**6,027,000**	4,881,000
Stockholders' Equity:		
Common stock — $.91 2/3 par value issued 5,901,996, outstanding 5,895,636 shares (after deducting 6,360 treasury shares)	**5,404,000**	5,404,000
Capital surplus	**6,145,000**	6,145,000
Retained earnings — Note 2	**145,154,000**	128,098,000
Stockholders' Equity	**156,703,000**	139,647,000
Total	**$260,529,000**	$229,813,000

Notes to Consolidated Financial Statements

1) Summary of Significant Accounting Policies

a) Principles of Consolidation

The consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries except for Mersco Finance Corporation. All intercompany accounts and transactions have been eliminated. The Company's investment in the finance subsidiary is carried at equity in its net assets.

Substantially all of the income before income taxes of Mersco Finance Corporation has been reflected in the Statements of Consolidated Income as a reduction of interest expense.

The consolidated statements include the equity in the earnings of affiliated companies owned 20% or more, which are joint ventures of the real estate subsidiaries.

The net current assets and results of operations of Canadian subsidiaries are included in the consolidated financial statements in terms of U.S. dollars on a dollar-for-dollar basis.

b) Accounts Receivable

Installment receivables maturing more than one year after January 31, 1974 and 1973 have been included in current assets in conformity with the usual practice followed by department store companies. Profit on installment sales is taken into income at the time of sale; carrying charges are recognized over the term of the installment contracts.

c) Inventory Pricing

Merchandise inventories, exclusive of merchandise in transit, are valued at the lower of cost or market by use of the retail inventory method applied on a first-in, first-out basis. Merchandise in transit is stated at cost and amounted to $26,062,000 in 1974 and $21,781,000 in 1973.

d) Depreciation

Buildings, improvements and fixtures are depreciated on a straight-line basis for book purposes. Accelerated depreciation is used for income tax purposes.

2) Retained Earnings

Under a loan agreement with an insurance company, payment of cash dividends on the common stock is limited to 70% of consolidated net income (as defined) subsequent to January 31, 1958. At January 31, 1974, the earnings free from this restriction were $55,539,000.

3) Mersco Finance Corporation

The Company sells its revolving and installment sales accounts to its finance subsidiary, Mersco Finance Corporation, without recourse. Mersco withholds, as a reserve, an amount equal to 10% of the receivables acquired. Mersco currently charges the Company a fee which is equal to one and one half times its fixed charges. Prior to July, 1972, all receivables purchased from the Company were sold to a bank.

The following are summary balance sheets for Mersco Finance Corporation:

	January 31, (in thousands)	
Assets	1974	1973
Customer receivables purchased from Mercantile Stores Company, Inc.	$ 57,587	$ 48,205
Equity in customer receivables sold (uncollected balances of $163,000 and $4,293,000, respectively)	16	429
Less—Amount payable to Mercantile Stores Company, Inc. pending collection of customer receivables	(5,775)	(5,250)
	51,828	43,384
Cash	16	20
Total Assets	$ 51,844	$ 43,404
Liabilities and Stockholders' Equity		
Current Liabilities		
Due to Mercantile Stores Company, Inc.	$ 47,257	$ 28,493
Due to bank	41	1,637
Federal income taxes	291	101
Accrued liabilities	115	—
	47,704	30,231
Long-Term Notes		
Due to bank	—	12,000
Due to affiliate	2,500	—
Stockholder's Equity	1,640	1,173
Total Liabilities and Stockholder's Equity	$ 51,844	$ 43,404

4) Leases and Commitments

See page 9 for information regarding leases and commitments.

Ten-year Review

Year ended January 31	1974	1973	1972
Operating Results			
Net sales	**$518,106,000**	$458,328,000	$393,258,000
Income before Federal income taxes	**40,695,000**	39,156,000	32,641,000
Percent to sales	**7.9**	8.5	8.3
Income before extraordinary item	**21,625,000**	20,756,000	17,251,000
Percent to sales	**4.2**	4.5	4.4
Extraordinary item	**—**	—	—
Dividends paid	**4,569,000**	4,127,000	4,127,000
Per Common Share			
Income before extraordinary item	**$ 3.67**	$ 3.52	$ 2.93
Extraordinary item	**—**	—	—
Dividends	**.77½**	.70	.70
Financial Position			
Working capital	**$ 95,248,000**	$ 88,127,000	$ 84,153,000
Ratio of current assets to current liabilities	**2.47**	2.73	3.14
Receivables—before deduction for accounts sold	**65,935,000**	65,473,000	52,673,000
Inventories	**87,139,000**	79,975,000	65,422,000
Property and equipment — net	**93,907,000**	87,368,000	76,538,000
Total assets	**260,529,000**	229,813,000	201,885,000
Long-term debt	**32,799,000**	34,243,000	35,819,000
Retained earnings	**145,154,000**	128,098,000	111,469,000
Stockholders' equity	**156,703,000**	139,647,000	123,018,000
Per common share	**26.58**	23.69	20.87
Return on stockholders' equity (1)	**14.6%**	15.8%	14.8%
Number of shares outstanding	**5,895,636**	5,895,636	5,895,636
Other Data			
Capital expenditures	**$ 16,072,000**	$ 19,766,000	$ 20,496,000
Depreciation	**9,533,000**	7,557,000	6,235,000
Number of stores	**72**	71	69
Total square feet	**7,372,000**	6,863,000	6,256,000

(1) Based on average of stockholders' equity at beginning and end of year.

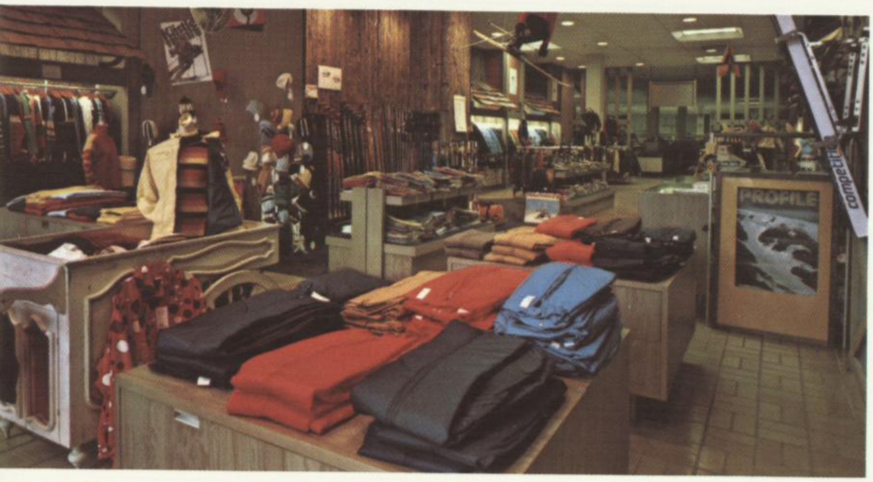
1971	1970	1969	1968	1967	1966	1965
$353,464,000	$318,353,000	$285,585,000	$256,550,000	$234,267,000	$220,610,000	$207,261,000
30,380,000	28,322,000	23,766,000	18,731,000	17,046,000	16,265,000	13,979,000
8.6	8.9	8.3	7.3	7.3	7.4	6.7
15,680,000	13,562,000	11,351,000	10,182,000	9,074,000	8,600,000	7,132,000
4.4	4.3	4.0	4.0	3.9	3.9	3.4
1,007,000	—	—	1,387,000	—	—	—
4,127,000	4,127,000	4,127,000	4,127,000	4,127,000	3,537,000	3,537,000
$ 2.66	$ 2.30	$ 1.93	$ 1.73	$ 1.54	$ 1.46	$ 1.21
.17	—	—	.24	—	—	—
.70	.70	.70	.70	.70	.60	.60
$85,501,000	$ 57,414,000	$ 52,679,000	$ 46,387,000	$ 43,829,000	$ 41,147,000	$ 38,651,000
3.27	2.75	2.66	2.80	2.79	2.57	2.68
47,740,000	43,807,000	41,615,000	38,309,000	35,949,000	34,748,000	34,106,000
57,975,000	50,321,000	46,017,000	39,757,000	33,325,000	32,179,000	30,124,000
63,052,000	54,622,000	52,171,000	48,319,000	44,157,000	42,031,000	40,714,000
188,844,000	146,898,000	137,726,000	121,909,000	113,949,000	111,387,000	104,439,000
37,268,000	14,102,000	15,731,000	13,526,000	14,572,000	15,858,000	16,177,000
98,345,000	85,785,000	76,350,000	69,126,000	61,684,000	55,705,000	51,674,000
109,894,000	97,334,000	87,899,000	80,675,000	73,234,000	67,255,000	63,223,000
18.64	16.51	14.91	13.68	12.42	11.41	10.72
15.1%	14.6%	13.5%	13.2%	12.9%	13.2%	11.6%
5,895,636	5,895,636	5,895,636	5,895,636	5,895,636	5,895,636	5,895,636
$ 14,178,000	$ 7,970,000	$ 8,178,000	$ 8,634,000	$ 6,887,000	$ 4,560,000	$ 3,771,000
5,182,000	4,613,000	4,326,000	3,983,000	3,485,000	3,243,000	3,413,000
66	62	61	61	60	58	60
5,656,000	5,134,000	5,005,000	4,942,000	4,630,000	4,427,000	4,447,000

joslins
OF COLORADO

It was the December of 1872. The rambling wood sidewalks of the Mile-High City of Denver bustled with Christmas shoppers. Denim clad miners, instantly wealthy from rich Rocky Mountain gold, rubbed shoulders with proper ladies attired in black silken dresses. As the Denver Pacific pulled in, John J. Joslin arrived to spend the holiday with his brother.

At 44, John J. was a successful man. Over the previous 20 years, he had established and built the largest business in his native Vermont: a mercantile emporium located in Poultney.

Impressed by the 14,000 inhabitants of this Colorado frontier town, J. J. later explained, "It was the climate and the character of the people I met and the fact that I thought there was a great future here that interested me in Denver." With his wife Mary and their three children, Joslin moved to Denver.



Sophisticate shop

He purchased the New York Dry Goods Store, a two-story building at the corner of 15th and Larimar, changed the name, and on April 22, 1873, three years prior to Colorado statehood, opened The Joslin Dry Goods Company. Located at the hub of the city, the building housed an unusual mixture. While the first floor hummed with the busy atmosphere of the increasingly successful mercantile establishment, boarders slumbered on the second.

Carrying the latest in stylish fashions and high-quality goods, Joslins built a reputation of customer satisfaction.

Elegantly furnished, the store drew many famous personages to its doors. Molly Brown browsed through the aisles, as did the newly wealthy, rough and tumble miners for whom nothing was too good. Baby Doe Tabor, accompanied by liveried footmen, would regularly draw up in front of the store and wait in her canopied carriage as the store employees hastened to the curbside to display silks and satins for her inspection.

By 1887, Joslins had outgrown its original location and moved uptown to 16th and Curtis. John J. requested that the building be constructed to meet the requirements of his business for many years to come. This landmark is still the headquarters of the seven present Joslin stores. In 1965, the original building was remodeled and expanded to offer six floors of well-displayed merchandise.

Since the early years, Joslins has been a spawning ground for other mercantile entrepreneurs. Past records reveal that a certain J. C. Penney was employed as a clerk in the Piece Goods Department in 1897 before founding the great retail empire that still bears his name.

SKI HAUS
uvex

In 1919, The Joslin Dry Goods Company became a member of the Mercantile Stores family. In fact, it was with Joslins that Mercantile Stores first began to experiment with branch stores. Starting in the 1940's, these store openings set the pace for the highly successful expansion in suburban areas throughout the country.

Denver's growth during the last quarter century has required that a second round of expansion be undertaken. Beginning in 1965, older stores that had become obsolete were replaced or remodeled and expanded. The Villa Italia store was opened in March, 1966 in the southeast quadrant of the city, replacing a smaller store in the same general area. This Joslin store is to be expanded from 80,000 to 140,000 square feet in the near future. A 100,000 square foot store was built in Cinderella City in Englewood in September, 1968, replacing a smaller store in the old downtown Englewood shopping district. In August, 1971, the 135,000 square foot Buckingham Square Aurora store was built, also replacing a smaller one in downtown Aurora. In February, 1969, the 100,000 square foot Crews Beggs Store in Pueblo, a separate Mercantile store, was brought into the Joslin family.

In July, 1973, a new 90,000 square foot Greeley store replaced a smaller store located in downtown Greeley. With the opening of this store, Joslins now serves all the residents of the Colorado front range—from Pueblo in the south to Greeley in the north—with modern Mercantile establishments.

Each Joslins store operates its own highly successful beauty salon, plus two free-standing salons.

From the beginning, Joslins has followed John J.'s philosophy of offering high fashion and quality merchandise. Besides featuring famous brand lines, Joslins has developed its own private label in order to offer its customers the best of two worlds—famous fashion brands combined with volume priced merchandise. This, along with a liberal exchange policy and guaranteed customer satisfaction, has served to reach a large segment of the retail market and gain the great reputation that has enabled Joslins to more than triple its retail space in the past decade.

With the steady growth of Colorado and the Denver area, Joslins is facing a great challenge and potential for further profitable growth in all areas of the state.

Today, with its good and well-deserved reputation for complete customer satisfaction, Joslins is a 100 year old tradition in Denver. Proud of its accomplishments, Joslins is also proud of its personnel. At the Downtown store, the average employee has been with the store for over eight years, while the buyers and management team have been employed for an average of 14 years. Without their great loyalty and effectiveness, Joslins' history of remarkable success and growth could not have been possible.

Colorado is an exciting, growing state with a pleasant climate and a great growth potential. Joslins is proud to be a major part of the Colorado retail scene.

In June, 1973, Joslins celebrated its 100th Anniversary —"A Century of Service." The vision of John J. Joslin was well on its way to being realized: "Joslins . . . the busiest store on the busiest corner of the busiest street of the busiest city in the West."

Mercantile Stores Company, Inc.

department store divisions

Bacons

Established 1845

Louisville, Kentucky
H. Marvin Dorethy, President
- Bashford Manor
- St. Matthew's
- Shively
- Jeffersonville, Ind.

GAYFER'S

Established 1879

Mobile, Alabama
Robert W. Holcomb, President
- Downtown Mobile
- Springdale
- Clearwater, Fla.
- Pensacola, Fla. (2)
- Tallahassee, Fla.
- Edgewater, Miss.
- Jackson, Miss.

Hennessy's

Established 1885

Butte, Montana
Milo D. Skordal, President
- Downtown Butte
- Helena

Glass Block

Established 1887

Duluth, Minnesota
William G. Stubenvoll, President
- Downtown Duluth
- Miller Hill

Castner Knott Co.

Established 1898

Nashville, Tennessee
James C. Lovell, President
- Downtown Nashville
- Donelson
- Green Hills
- Harding Mall
- Rivergate
- Shelbyville
- Bowling Green, Ky.

joslins

Established 1873

Denver, Colorado
Donald R. Chabot, President
- Downtown Denver
- Aurora
- Boulder
- Englewood
- Greeley
- Pueblo
- Villa Italia

the Jones Store co.

Established 1887

Kansas City, Missouri
Ronald W. Ferguson, President
- Downtown Kansas City
- Blue Ridge
- Overland Park, Kans.
- Pittsburg, Kans.
- Prairie Village, Kans.

Peoples

Established 1888

Tacoma, Washington
Henry W. Powell, President
- Downtown Tacoma
- Lakewood
- Olympia (Lacey)
- Port Angeles
- Wenatchee
- Yakima

GAYFER'S MONTGOMERY FAIR

Established 1868

Montgomery, Alabama
Stephen E. Maxwell, President
- Montgomery
- Auburn
- Eastbrook
- Tuscaloosa

Root's

Established 1856

Terre Haute, Indiana
Frank C. Schrohe, President
- Downtown Terre Haute
- Honey Creek
- Sullivan
- Robinson, Ill.

de Lendrecie's

Established 1879

Fargo, North Dakota
Ray Klein, President
- Fargo

Lazarus

Established 1889

Wilkes-Barre, Pennsylvania
Stanley R. Dahlgren, President
- Downtown Wilkes-Barre

White's

Established 1874

Columbia, South Carolina
Thomas E. Hale, President
- Richland Mall
- Dutch Square

Lion

Established 1857

Toledo, Ohio
Philip W. Kaiser, President
- Downtown Toledo
- Southwyck
- Westgate

The Right House

Established 1843

Hamilton, Ontario, Canada
Russell W. Lackie, President
- Downtown Hamilton
- Brantford
- Cambridge
- Guelph
- St. Catharines

White's

AUGUSTA'S PACE SETTER

Established 1874

Augusta, Georgia
Robert W. Tyler, President
- Downtown Augusta
- National Hills
- Aiken, S. C.

McAlpin's

Established 1852

Ohio Operations
David R. Huhn, President
- Downtown Cincinnati
- Cherry Grove
- Kenwood
- Middletown
- Northgate
- Western Hills

Kentucky Operations
Ralph T. Glassford, President
- Lexington, Ky. (2)

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20 Pine Street
New York, N. Y. 10015

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First National City Bank
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